

UNITED STATES OF AMERICA
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Before Commissioners:

Robert G. Taub, Chairman;
Michael Kubayanda, Vice Chairman;
Mark Acton;
Ann C. Fisher; and
Ashley E. Poling

Periodic Reporting
(UPS Proposal One)

Docket No. RM2020-9

PUBLIC REPRESENTATIVE COMMENTS ON UPS PROPOSAL ONE

December 15, 2020

I. EXECUTIVE SUMMARY

The Public Representative respectfully submits the following comments on UPS' Petition to "...modify the analytical principles for determining incremental costs under 39 U.S.C. § 3633(a)(1) and 39 U.S.C. § 3633(a)(2) to address the failure of the existing costing models to consider and attribute the increased costs resulting from the Postal Service's seasonal spike in operations."¹ Petition at 5.

The Petition requests the Commission to attribute unexplained peak-season costs to competitive products as part of group incremental costs and to revise cost models to account for seasonality effects by assigning them to competitive incremental

¹ Docket No. RM2020-9, Petition of United Parcel Service, Inc. for the Initiation of Proceedings to Make Changes to Postal Service Costing Methodologies, May 29, 2020 (Petition).

costs or to each competitive product. Underlying the Petition's recommendations is the argument that competitive products are the sole, or nearly the sole, factor causing the extra costs associated with peak periods. The Public Representative does not find UPS' evidence supporting this claim to be convincing. He also agrees with the Postal Service that the Petition's calculation of unexplained costs is faulty.

The Public Representative supports the basic idea of the Postal Service that one should undertake a set of pre-estimation tasks before developing models which might capture a seasonal or peak effect in the cost segment to which a cost model is applied. He recommends the Commission open a Public Inquiry which further develops the set of pre-estimation tasks to assist whether or not to develop peak models and if so, what types of models and cost drivers are appropriate given the set of operational factors driving peak costs. The Public Representative believes it is important for the Commission to establish guidelines before parties recommend ad hoc and/or inconsistent modeling of peak season costs.

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II. INTRODUCTION

A. UPS' Petition And Materials Presented At Technical Conference

UPS' Petition raises two major issues. First, it states that existing "costing models fail to explain and attribute approximately \$500 million of the additional costs caused to meet peak-season demand." Petition at 3. Second, it states that "[t]he Commission has not yet evaluated the full set of costs the Postal Service could eliminate through an efficient reorganization of its delivery network and other aspects of its operations if it ceased delivering competitive products. Ibid. It avers the calculation of these costs should be considered to be incremental competitive costs, which should be paid by, or attributed to, consumers of competitive products. Id. at 4.

Consequently, UPS requests the Commission to direct the Postal Service to:

"Attribute unexplained peak-season costs to competitive products as part of group incremental costs; revise cost models to account for seasonality effects, and produce various types of peak-season operational data to permit improved cost attribution to competitive products and a more accurate measure of competitive incremental costs." Id. at 3-5, 38.

UPS' Petition, as well as the materials it presented at the Technical Conference (UPS Materials),² present evidence on several problems caused by the failure to properly incorporate a December peak in the Postal Service's cost models. In particular, this failure results in improper cost attribution and improper determination of competitive incremental costs. UPS also suggests various remedies and additional data collection.

B. Technical Conference

On July 13, 2020, the Commission established this docket, scheduled a technical video conference to be held on September 29, 2020, and identified questions and

² Docket No. RM2020-9, Notice of Materials to Be Used in Technical Conference, Seasonal Increases in US Postal Service Costs Driven by Competitive Products, Presentation to Postal Regulatory Commission for Technical Conference (UPS Materials), filed September 28, 2020.

issues it wanted UPS to address and other issues it wanted the Postal Service to address.³

C. USPS' Technical Conference Presentation (Materials)

On September 28, 2020, the Postal Service filed materials it presented at the September 29, 2020 Technical Conference.⁴ In its Petition and Materials, UPS develops a method to calculate costs which are not captured by the Postal Service's existing cost models ("unexplained costs"). In the Technical Conference, the Postal Service argued that UPS' method forecasts monthly volume variable costs using average annual unit accrued costs. USPS argues this approach substantially overstates the peak change in institutional costs. USPS Materials at 21-22. The Postal Service calculates that unexplained accrued costs for the December peak are approximately \$242 million, less than one-half the magnitude, of UPS' calculation. *Ibid.*

The Postal Service also discusses different methods of calculating seasonal attributable and incremental costs, and provides a research "checklist" to determine whether additional data needs to be gathered, whether existing cost models can be easily modified to include seasonal effects, or whether new model(s) and data are necessary to capture seasonal effects. *Id.* at 24.

III. UPS' ARGUMENTS

A. The Seasonal Cost Spike Is Caused By Competitive Products

1. General Arguments

UPS notes that the costs caused by competitive products' use of Postal Service capital and labor from each cost component are driven by factors which are non-volume

³ Docket No. RM2020-9, Postal Regulatory Commission, Notice And Order Establishing Docket To Obtain Information Regarding Proposed Changes To Cost Methodologies And Scheduling Technical Conference, July 13, 2020.

⁴ Docket No. RM2020-9, Response of The United States Postal Service to Order No. 5687 Regarding Technical Conference Material (USPS Materials), filed September 28, 2020.

bigger, bulkier, and heavier than envelopes. This is especially true for processing, transportation, and delivery activities. Petition at 1.

Its Petition argues that the increase in December demand for the functions performed by Postal Service capital and labor are driven exclusively by competitive products. Specifically, it argues that the Postal Service

“...hires tens of thousands of temporary workers, opens temporary delivery annexes, incurs additional overtime wages, and sends carriers out on a host of additional runs to deliver packages. These increased costs are a clear example of costs that should be attributed to competitive products under the principle of incremental-cost attribution adopted by this Commission.” *Id.* at 2.

UPS goes on to argue that increased December costs should be considered to be caused solely by competitive products because the increase in costs between November and December would not exist but for the need to handle, process, and deliver packages, which are competitive products. *Id.* at 3. UPS also suggests that the growth of competitive products has caused the Postal Service to reconfigure major cost functions, such as mail processing, use of building space, vehicle maintenance and use, transportation, delivery, etc. Consequently, it requests the Commission estimate the network reconfiguration costs solely caused by the growth in competitive products, and consider them to be competitive incremental costs, which should be paid for by consumers of competitive products under 39 U.S.C. § 3633(a)(1), 39 U.S.C. § 3633(a)(2), and 39 U.S.C. § 3633(a)(3) of the Postal Accountability and Enhancement Act (PAEA).⁵ *Id.* at 4, 5 (fn. 5).

⁵ See, Postal Accountability and Enhancement Act (PAEA). 39 U.S.C. § 3633(a)(1) of the PAEA specifies the requirement for the Commission to prohibit the subsidization of competitive products by market-dominant products; 39 U.S.C. § 3633(a)(2) specifies the requirement for the Commission to ensure that each competitive product covers its attributable costs; and 39 U.S.C. § 3633(a)(3) requires the Commission to ensure that competitive products collectively cover what the Commission determines to be an appropriate share of the institutional costs of the Postal Service.

2. Quantitative Evidence That Package Volumes and Costs Are The Primary Cause Of Peak Monthly Costs In December

UPS presents uncontroversial evidence that volumes and costs for various activities reach a peak in the month of December. See, e.g., *Id.* at 6-13. To make the case that peaks in December volumes and costs are solely, or at least primarily, caused by packages, UPS presents charts which show that package volumes and city carrier costs appear to be highly correlated by month over the last six years.⁶ *Id.* at 14. UPS also presents a chart of the standardized daily volume of packages, First Class Mail, Periodicals, and Marketing Mail, which shows that although First Class Mail reaches a volume peak in December, Package Mail achieves a higher and growing, standardized peak in December volume from 2018 to 2019. *Id.* at 16. Finally, UPS presents two figures which show the December volumes for First Class Mail and Packages from FY 2016 to FY 2019. First Class Mail volumes decreased from approximately 6.1 billion pieces to 5.5 billion pieces, while Package volumes increased from 553 million pieces to 644 million pieces. UPS Materials at 5-6.

B. UPS Claims Postal Service Cost Models Fail To Account For Hundreds Of Millions Of Dollars In Peak Season Costs

UPS develops a method to quantify the extent to which existing cost models fail to fully account for December (Peak) costs, by comparing *predicted* increases in *volume variable costs* from November to December, to *actual* increases in *accrued costs* from November to December (by cost segment and mail class). The Notation and Equation 1 below enumerate the formula UPS uses to calculate the difference between estimated cost increases between November and December and actual cost increases between

⁶ UPS also shows the costs of Special Route (SPR) Drivers hits a peak in December. The Commission recently accepted an SPR cost study, which was undertaken in response to the growing number of SPR Routes whose carriers delivered packages. The study accounted for a seasonal December peak, and resulted in a \$124.7 million increase in attributable costs for domestic competitive mail products and in a decrease of \$67.8 million in attributable costs for domestic market dominant mail products.” See, Docket No. RM2019-6, Order No. 5405, Order On Analytical Principles Used In Periodic Reporting, Proposal One, January 14, 2020. UPS’ Petition does not discuss whether or not, and to what extent, the new SPR methodology adequately address its concerns.

November and December. Unexplained cost change is the difference between the actual change in accrued costs and the estimated change in accrued costs. See, UPS Materials at 12.

Notation For UPS' Unexplained Cost Calculation: (See, UPS Materials at 12)

- Upper case letters refer to annual totals, lower case to monthly values.
- A represents volume variable and product specific costs.
- c represents total (accrued) costs.
- V represents annual volume, and v represents monthly volume.
- n represents November, d represents December.
- j indexes cost categories, including clerks, delivery, transportation, and other.
- k indexes mail classes.

u_j , the unexplained December cost increase for cost category j is given by:

$$u_j = (c_{jd} - c_{jn}) - \sum_k \frac{A_{jk}}{V_{jk}} (v_{kd} - v_{kn}) \quad \text{Equation 1}$$

UPS estimates that current costing models fail to explain and attribute approximately \$500 million of the additional peak-season costs incurred by the Postal Service on average, between 2016 and 2019. Petition at 24. Because the volume variable costs of several major cost segments are determined by variability cost studies, UPS draws two conclusions from its estimate of unexplained cost changes between November and December. First, the magnitude of unexplained attributable costs suggests that the Postal Service does not have a method to identify competitive incremental costs which are greater than individual cost the attribution of competitive products by enough to account for its estimate of unexplained seasonal costs. Petition at 25, and 25 (fn. 40). Second, the Postal Service's cost models do not account for the additional resources used during the December peak, the additional costs of which UPS considers to be incremental competitive costs.

C. UPS' Claim That Several Of the Postal Service's Major Costing Models Fail To Adequately Account For The December Peak And So Underestimate Incremental Competitive Costs.

UPS points to a number of instances where the Postal Service's variability cost models do not properly account for the December spike on costs associated with competitive products.

The Current City Carrier Model does not account for seasonality. Sample package data are drawn from 13 days in the spring of 2014. *Id.* at 29.

Very few Form 3999 route evaluations, which form the basis for the development of carrier cost pools, are taken during December. *Id.* at 31.

Costs associated with deploying resources to accommodate a December peak, which UPS terms "start-up costs," should be considered incremental to the mail class responsible for the December or seasonal peak, rather than recorded as an accrued cost to which a variability factor is applied. UPS Materials at 23.

D. UPS' Recommendations

1. UPS Requests The Commission Require The Postal Service To Develop Cost Models Which Take Seasonality Into Account

UPS makes several recommendations with regard to the treatment of peak costs. One recommendation is based on the reasonable observation that sample data should be representative of all months in a year, and not limited to sample period based on "average" activity, e.g., modeling city carrier street time variability using monthly data, Petition at 29-33. UPS also supports the Postal Service's Special Route Study (SPR), which after examining the operational features of SPR delivery, such as whether or not the SPR route was located in a normal or a small location, and seasonality, developed eight regression models.⁷ UPS also reasonably requests that the seasonal aspects of transportation variability take into account seasonal "Christmas Routes." *Id.* at 34-35.

⁷ See, Docket. No. RM2019-6, Petition of the United States Postal Service for the Initiation of a Proceeding to Consider Proposed Changes in Analytical Principles (Proposal One), June 21, 2019, at 28-39

2. UPS Requests the Commission To Require The Postal Service To Produce Disaggregated Data To Better Study The Impact Of Peak Periods On Costing

UPS also recommends the Commission request the Postal Service to produce a variety of fairly disaggregated data to better inform research on the impact of peak season volumes on costing. Such data would include: monthly product-level delivery volumes, by shape, broken down by city carrier letter routes, city carrier SPRs, and rural carrier routes; microdata from the CCCS, the CCCS-SPR, the RCCS, IOCS, MODS, and TRACS, and other data systems, with product-level detail and time stamps intact; as well as monthly estimates of SPR and letter route costs. *Id.* at 33.

3. UPS Requests The Commission To Attribute Start-up Costs To Competitive Products

UPS's requests the Commission consider all "start-up" seasonal costs as being solely caused by competitive products, and therefore treat them as incremental competitive costs. Start-up costs occur when there is extraordinarily high "volume growth during a peak season which forces the Postal Service to take special actions and set up temporary operations to accommodate the peak....When actions such as this occur, any startup costs and/or fixed costs associated with these temporary operations should be attributed to the products experiencing the volume increases that make these temporary operations necessary." *Id.* at 35.

4. UPS Requests The Commission Attribute Unexplained Costs To Competitive Products As A Whole, Or To Individual Competitive Products According To Each Product's Weighted Share Of Competitive Product Volume.

The Public Representative discussed UPS' method of determining the magnitude of unexplained seasonal costs in Section III.B above. It estimated that the average unexplained costs between 2016 and 2019 was approximately \$500 million. UPS requests the Commission to treat these unexplained seasonal costs as incremental competitive costs. In the event, the Commission does not do so, UPS requests the

Commission to attribute unexplained season costs to individual competitive products according to each products' share of the total competitive volume times weight. Id. at 40.

IV. POSTAL SERVICE'S ARGUMENTS

A. USPS Argues The Seasonal Cost Spike Is Caused By Competitive And Market Dominant Products

The Postal Service's arguments were presented in the Technical Conference held September 29, 2020, and submitted to the Commission the day before. The Postal Service disagrees with UPS's contention that all peak season costs are (primarily) caused by the delivery of competitive products. It first presents graphical data showing that the volumes of both First Class and Competitive Mail have a December peak greater than November volumes.

More to the point, the data show that the increase in First Class mail volumes from November to December exceed November to December growth in competitive mail volumes by a factor six in 2017 and a factor of eight in 2018 and 2019. USPS Materials at 9. The story is similar with respect to First Class and Competitive December mail volumes from 2016 to 2018. First Class Mail volumes in December exceeded Competitive mail volumes in December by factors of eleven and twelve. Id. at 8. The Postal Service concludes its discussion of this issue by stating that "competitive volumes are a contributor to seasonal peak costs, but are certainly not the sole cause." Ibid.

B. USPS Argues That UPS Overstates The Amount of Unexplained Peak Season Cost By One-Half

The Postal Service maintains that UPS over-estimates unexplained changes in costs between November and December, because it is comparing the change in accrued costs from November to December to the change in volume from November to December, multiplied by the average annual unit volume variable cost. The Postal Service argues that UPS' formula (see Equation 1 in these Comments) multiplies the

average annual volume variable cost per piece (which is constant over year) by the change in volumes from November to December. And because it then compares this calculation to the relatively high, peak change in accrued costs from November to December, there appears to be a large “unexplained amount.” USPS argues that this occurs because using average annual volume variable unit cost term in Equation 1,

$\sum_k \frac{A_{jk}}{V_{jk}}$, understates the estimate of the November to December change in explained

costs, and so overstates the calculation of unexplained costs. *Id.* at 18.

C. The Operational Response To Volume Peaks Determines How Seasonal Product Costs Should Be Calculated

The Postal Service presents a set of pre-estimation tasks which should be undertaken before developing models which might capture a seasonal or peak effect operating in the cost segment to which a cost model is applied. Specifically, the Postal Service recommends that the extent to which operations and/or volumes differ in peak and non-peak periods should be the basis for the types of models an analyst should first consider. For example: if existing resources and methods are used more intensively during the peak, but operations remain essentially unchanged, then it is probably not necessary to alter the structure of the existing cost model. *Id.* at 11. If resources and operations are used more extensively during the peak, then operations may change to the point it makes sense to consider altering the cost model.⁸ *Ibid.* Finally, if a December peak for a cost segment, whose variability is estimated by a cost model, uses new types of resources and/or operations, then one should investigate the appropriateness of developing a new model structure.⁹ *Ibid.*

⁸ The Public Representative bases his discussion of these three steps on the Postal Service’s Technical Conference Materials. He has stated the difference between the three operational conditions in his own terms.

⁹ These same principles are stated in a similar form on page 24.

V. PUBLIC REPRESENTATIVE COMMENTS

A. Introduction

The Public Representative appreciates the efforts UPS made to document the ways in which the growth of competitive products, especially growth during the peak demand month of December, can complicate cost attribution. He is sympathetic to UPS' ongoing concern that the growth of competitive products will increasingly drive investment, labor, and operational design changes which will best promote the expansion of competitive products, even if these same operations, investments, and labor are also used by market dominant products.¹⁰ Proper consideration of this type of cost causation is best handled through a long run, forward-looking, incremental cost analysis.¹¹ Unfortunately, prior Commission decisions have not considered forward-

¹⁰ This concern is not new, and is long-recognized as a complicating factor for setting prices and costs when products with different design and use features use the same infrastructure. For example, the higher weight of shipping trucks, compared to residential vehicles, suggests the need for owners of shipping trucks to pay a greater user fee per mile (i.e. for apparently the same use) than owners of residential vehicles. "America moves on its roads and these roads are in trouble. They are deteriorating at an accelerated pace and are not capable of meeting current needs or meet future requirements. While there are many uncontrollable causes of highway deterioration, such as weather, excessive truck weight is one cause which can be controlled." See, United States Government Accountability Office (GAO), Excessive Truck Weight: An Expensive Burden We Can No Longer Support, CED-79-94, July 16, 1979, at 1.

¹¹ The Federal Communications Commission (FCC) adopted a variant of a forward-looking, long run, incremental cost model, when it adopted the total element long run incremental cost (TELRIC) method of determining the cost, and therefore (access) price of a component or "element," of an incumbent Local Exchange Company's (LEC) network. See, e.g., Federal Communications Commission, CC Docket No. 96-98, Implementation of the Local Competition Provisions in the Telecommunications Act of 1996 and CC Docket No. 95-185, Interconnection between Local Exchange Carriers and Commercial Mobile Radio Service Providers, First Report And Order, FCC 96-325, August 8, 1996, at para. 675. "Incremental costs are forward-looking in the sense that these costs are incurred as the output level changes by a given increment....The incremental cost of connecting a new residence to its end office, however, is the cost of the loop. Forward-looking incremental costs, plus a portion of the forward-looking joint and common costs, are sometimes referred to as 'economic costs.' Embedded or accounting costs are costs that firms incurred in the past for providing a good or service and are recorded as past operating expenses and depreciation. Due to changes in input prices and technologies, incremental costs may differ from embedded costs of that same increment. In competitive markets, the price of a good or service will tend towards its long-run incremental cost."

looking incremental cost method.¹² Rather, it has adopted the short run, embedded-cost, (backward-looking) incremental cost method, first developed in R2000-1.¹³ Consequently, UPS has been left little choice but to “shoehorn” the cost impacts which might be measured by long-run, forward-looking, incremental costs into other issues, such as seasonality and peak demand.

The Public Representative also appreciates the Postal Service’s discussion of criteria which should be used to determine the types of peak demand models which would be most appropriate under various demand and operational conditions. He also appreciates the Postal Service’s discussion of the features of UPS’ “unexplained cost” analysis, and its presentation of absolute, un-indexed, volumes of First Class Mail compared to Competitive Products and Services.

B. Assessment of UPS’ Petition and Materials

1. Peak Period (December) Postal Service Costs Are Not Incremental Competitive Costs

Perhaps the most consistent theme expressed in UPS’ Petition and Materials is the notion that peak season costs, in particular costs the Postal Service incurs in December, are incremental competitive costs. UPS states its position in the early pages of its Petition:

“[p]eak-season costs... are caused by competitive products, but largely overlooked by, existing costing methodologies.... These costs arise because, to meet the December spike in demand for package delivery services, the Postal Service hires tens of thousands of temporary workers, opens temporary delivery annexes, incurs additional overtime wages, and sends carriers out on a host of additional runs to deliver packages.... Peak-season costs plainly qualify as incremental costs of the package delivery business under this standard. Such costs *would not exist* if the

¹² See, e.g. Docket No. RM2017-1, Order No. 4963, Order Adopting Final Rules Relating To The Institutional Cost Contribution Requirement For Competitive Products, January 3, 2019, at 28.

¹³ See, Docket No. R2000-1 Postal Rate and Fee Changes, 2000, United States Postal Service, USPS-T-22, Direct Testimony Of Michael D. Bradley On Behalf Of United States Postal Service, January, 12, 20000.

Postal Service did not deliver packages.” (Original emphasis). UPS Petition at 2-3.

UPS fails to provide convincing evidence to substantiate its claim that peak season costs are caused, either solely or primarily, by competitive products. Some of its claims are merely asserted without documenting that peak season competitive products are solely or primarily responsible for the increased costs incurred during peak season. See, e.g. UPS Petition at 3, 5 (fn. 5), 13.

UPS also produces a number of graphs which purport to document this relation. In particular, UPS compares the indexed rates of growth of competitive products to market dominant mail products, such as First Class Mail, Marketing Mail, and Periodicals. UPS Petition at 16, 18. However, the Postal Service shows that market dominant products, in particular First Class Mail also has a December Peak and First Class Mail has much larger share of December mail volume than competitive products. The Postal Service also shows that indexed measures of growth accentuate the growth rates of products with small volumes. One naturally obtains a much larger rate of volume change when using a small starting base compared to a large starting base. See, USPS Materials, at 7-9.

2. UPS' Unexplained Peak Cost Method Is Flawed

The Public Representative reproduced the formula for calculating unexplained seasonal costs in Equation 1, above. Equation 1 is reproduced here for the sake of convenience

$$u_j = (c_{jd} - c_{jn}) - \sum_k \frac{A_{jk}}{V_{jk}} (v_{kd} - v_{kn}) \quad \text{Equation 1}$$

Equation 1 compares the difference between the change in accrued costs between November and December to the estimated change in volume variable costs between November and December. The latter estimate is obtained by multiplying average annual unit volume variable costs by the change in mail volume between November and December. USPS Materials at 12.

There are two problems with Equation 1. First, comparing an estimated change in *volume variable costs* (between November and December) to the actual change in *accrued costs* during the same time, can at best measure only the change in institutional costs during this time period (emphasis added). The method might reveal meaningful results if UPS' estimate of unexplained (institutional) costs between November and December, was compared to the actual change in institutional costs during the same time period. But UPS does not do this. In the opinion of the Public Representative, UPS' calculation does not provide clear decision rules for policy-making.¹⁴

Moreover, the Postal Service shows that UPS' estimate of the change in volume variable costs is understated because it uses *average annual* unit volume variable costs, rather than the *average monthly* unit volume variable cost change between November and December. Doing so, overstates the difference between the monthly accrued cost change and the estimated peak change in volume variable costs.¹⁵ USPS Materials at 19. Because the actual change in volume variable costs between November and December is almost certainly greater change in volumes between November and December multiplied by annual average unit volume variable costs, the estimated change in volume variable costs between November and December is *less* than it should be in order to be properly compared to the change in accrued costs between November and December. Conversely, the magnitude of unexplained changes in institutional costs between November and December is overstated.

¹⁴ To be fair, it should be noted that the alternate method used by the Postal Service yields a much lower estimate of unexplained costs, but its method still yields a positive value for unexplained institutional costs between November and December. In order to provide a reasonably accurate estimate of the change in institutional costs during December, it would be necessary to develop variabilities for all cost segments for the month of December. This would be a major undertaking in the opinion of the Public Representative, and would only be justified if one believed that all costs above average costs, which are incurred in December, are caused solely by competitive products.

¹⁵ In other words, UPS' method overstates the "unexplained change."

3. UPS' Request To Attribute Start-Up Costs To Competitive Products Is Misplaced

UPS requests the Commission attribute start-up costs solely to competitive products, either as a group of products as a whole, in which case start-up costs could be treated as incremental competitive costs, or to individual competitive products, according to each products' share of competitive volume multiplied by the weight of competitive products.

Both requests require the Commission to accept UPS' argument that all peak and/or unexplained costs are caused solely by competitive products. As he previously discussed, the Public Representative finds the Postal Service comparison of First Class Mail volumes growth compared to Competitive volumes and growth convincing evidence that competitive products do not solely, or even primarily, cause peak season or peak month costs. The Commission should reject all requests to exclusively attribute costs to competitive products made on this basis.

4. The Postal Service's Pre-Model Inquiry Template Is A Useful Tool To Identify Types Of Model Changes Needed To Incorporate Seasonality Into Cost Models

The Postal Service develops a "template" of operational seasonal or peak changes to consider to help determine what type of model changes might be correspondingly appropriate. It identifies three type of operational changes to consider, and suggests a corresponding type of change in cost models. First, if the existing operations during a peak season versus average seasons are used more intensively in a cost model, the Postal Service would recommend to continue using+ the established model structure, supplemented by modest changes in variables and data. An example might involve estimating volume variability(ies) in an existing cost model separately for peak and non-peak periods.

So, e.g., one might be able to estimate the existing city carrier model during peak and non-peak periods using the same shape data, but collecting during two sample periods. Each shape variable would probably have different peak and non-peak variability estimates. Distribution keys for the two periods would also differ, although they would continue to be based on product volumes. USPS Materials at 14-15.

Second, if the function being modelled uses new types of resources and/or methods during the peak period, the Postal Service would recommend investigating whether a new model structure is required. Ibid. Third, if the function being modelled uses additional amounts of existing resources and methods, the Postal Service states that the change in the cost model depends on the magnitude of additional resources used by this cost function. Ibid.

However, the Postal Service does not explore whether a large, peak season, change in the magnitude of resource use is best accommodated by the same model structure, or whether a new model structure would be more appropriate. The recommendation appears to imply that an analyst should examine the magnitude of the increased resource use, determine whether the change in magnitude is sufficient to require a model change, or whether it the change in the magnitude of resources use requires a change in operational structure which would also require a change in model structure.

The Public Representative believes that whether resource use is more intense or more extensive, the change may be sufficient to require a model change. He supports

using changes in resources and operations when considering whether a model change is appropriate. For any of the operational and/or resource use changes the Postal Service identifies, it will be necessary to provide relevant data at a level no greater than the monthly level.¹⁶ It would probably be advisable to provide data at an even more disaggregated level, in order to check the stability of proposed model changes, as well as the quality of monthly data.

VI. CONCLUSION

For the reasons enumerated in the above discussion, the Public Representative requests the Commission to adopt his recommendations.

Respectfully Submitted,

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¹⁶ For this reason, the Public Representative believes UPS' request for disaggregated data is reasonable, once one begins the process of considering a model change to accommodate peak demand.